

BEFORE THE DEPARTMENT OF ADMINISTRATION
OF THE STATE OF MONTANA

In the matter of the amendment of ARM)	NOTICE OF PUBLIC HEARING
2.59.1701, 2.59.1703, 2.59.1705,)	ON PROPOSED AMENDMENT,
2.59.1706, 2.59.1707, 2.59.1709, and)	REPEAL, AND ADOPTION
2.59.1710 pertaining to the licensing and)	
regulation of mortgage brokers, mortgage)	
lenders, and mortgage loan originators;)	
the repeal of ARM 2.59.1704, 2.59.1711,)	
2.59.1712, 2.59.1713, and 2.59.1715;)	
and the adoption of NEW RULES I)	
through VIII regarding license renewals)	
for mortgage lenders as of July 1, 2009;)	
new applicants for a mortgage loan)	
originator license – temporary licenses;)	
new applicants for a mortgage broker or)	
mortgage lender license – temporary)	
licenses; net worth requirement for)	
mortgage brokers; unacceptable assets;)	
proof of net worth; records to be)	
maintained by mortgage lenders and)	
financial responsibility)	

TO: All Concerned Persons

1. On September 3, 2009, at 10:00 a.m., a public hearing will be held in Room 342 of the Park Avenue Building, 301 S. Park, Helena, Montana, to consider the proposed amendment, repeal, and adoption of the above-stated rules.

2. The Department of Administration, Division of Banking and Financial Institutions, will make reasonable accommodations for persons with disabilities who wish to participate in this public hearing or need an alternative accessible format of this notice. If you require an accommodation, contact the Division of Banking and Financial Institutions no later than 5:00 p.m. on August 31, 2009, to advise us of the nature of the accommodation that you need. Please contact Christopher Romano, Division of Banking and Financial Institutions, P.O. Box 200546, Helena, Montana 59620-0546; telephone (406) 841-2928; TDD (406) 444-1421; facsimile (406) 841-2930; e-mail to cromano@mt.gov.

3. The rules proposed to be amended provide as follows, stricken matter interlined, new matter underlined:

2.59.1701 DEFINITIONS For purposes of the Montana Mortgage Broker, Mortgage Lender, and Mortgage Loan Originator Licensing Act and this subchapter, the following definitions apply:

(1) remains the same.

~~(2) "Conviction" means a judgment of conviction or sentence entered upon a plea of guilty or nolo contendere or upon a verdict or finding of guilty of an offense rendered by a legally constituted jury or by a court of competent jurisdiction authorized to try the case without a jury.~~

~~(3) "Employed by" means:~~

~~(2) "Employing" means the entity for whom the individual works is liable for withholding payroll taxes pursuant to Title 26 of the United States Code.~~

~~(a) an individual performing a service for a mortgage broker liable for withholding taxes pursuant to Title 26 of the United States Code; or~~

~~(b) any individual acting as an independent contractor for a mortgage broker if that individual is under exclusive written agreement to broker loans only through their sponsoring mortgage broker or if the sponsoring mortgage broker undertakes accountability for the regulated mortgage loan activities of the independent contractor.~~

~~(4) "Fraud or dishonesty" means, but is not limited to:~~

~~(a) a conviction, under the laws, rules, or regulations of any state or the federal government, that relates to fraud or dishonesty; or~~

~~(b) a conviction that involves robbery, illegal gambling, receiving stolen property, counterfeiting, extortion, check, credit card, or computer violations set forth in criminal laws, deception, fraud, theft, embezzlement, defrauding a creditor, issuing a bad check, deceptive practices, deceptive business practices, misappropriation of funds or property, misrepresentation, omission of material facts, unauthorized use of property, forgery, identity theft, or money laundering.~~

~~(5) "Fraudulent or dishonest dealings" means, but is not limited to:~~

~~(a) a civil judgment, under the laws, rules, or regulations of any state or the federal government, that relates to fraud or dishonesty; or~~

~~(b) a civil judgment that involves deception, fraud, conversion, misappropriation of funds, misrepresentation, omission of material facts, forgery, unauthorized use of money or property, failure to pay taxes, or bad checks.~~

~~(6) and (7)(a) through (h) remain the same, but are renumbered (3) and (4)(a) through (h).~~

~~(i) any change which would cause have authorized the department not to issue a license, if it had occurred before licensure.~~

~~(8) "Mortgage broker entity" means corporation, limited liability corporation, partnership, limited liability partnership or any other organization other than a sole proprietorship.~~

~~(9) and (10) remain the same, but are renumbered (5) and (6).~~

~~(7) "Termination" means separation from employment for any reason. The term includes the circumstance of a loan originator when the employing entity's Montana license is suspended, revoked, or surrendered even though the loan originator may continue to be employed by the entity in another capacity or in another state.~~

~~(14) (8) "Work in a related field" or "in a related field" means:~~

~~(a) for a mortgage broker designated manager, three years:~~

~~(i) as a mortgage broker, or a branch office manager of a mortgage broker business;~~

- (ii) as a mortgage banker, or responsible individual or branch manager of a mortgage banking business;
- (iii) as a ~~real-estate~~ mortgage loan officer;
- (iv) as a branch manager of a ~~real-estate~~ mortgage broker or lender;
- (v) as a mortgage loan originator; or
- (vi) as a state or federal regulator who examines compliance of residential mortgages of state or federally chartered financial institutions; or
- ~~(vi)~~ (vii) as a mortgage ~~broker~~ loan originator licensee in another state where the licensing standards are substantially similar to those in this state, as determined by the department; and
- (b) for a mortgage loan originator, six months:
 - (i) as a loan originator in a mortgage broker business;
 - (ii) as a loan originator in a mortgage banking business;
 - (iii) as a ~~real-estate~~ mortgage loan officer;
 - (iv) as a mortgage loan originator licensee in another state where the licensing standards are substantially similar to those in this state, as determined by the department;
 - (v) as a ~~real-estate~~ mortgage loan processor;
 - (vi) as a ~~residential-real-estate~~ mortgage loan closing agent; or
 - (vii) remains the same.

AUTH: 32-9-125, 32-9-130, MCA

IMP: ~~32-9-103~~, 32-9-109, ~~32-9-115~~, 32-9-116, 32-9-117, 32-9-122, 32-9-123, 32-9-125, 32-9-133, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to amend the first sentence of this rule to reflect the revised title of the Montana Mortgage Broker, Mortgage Lender, and Mortgage Loan Originator Licensing Act (the Act).

The department proposes to repeal the definitions of "conviction," "fraud or dishonesty," "fraudulent or dishonest dealings," and "mortgage broker entity" because these definitions are no longer needed under the Act. The terms "fraud or dishonesty" and "fraudulent or dishonest dealings" are no longer used in the Act. The terms "conviction" and "mortgage broker entity" are defined directly or indirectly in 32-9-120, MCA, and 32-9-103, MCA, respectively.

Subsection (4)(i) is being amended for clarification purposes because what might have caused the department to deny licensure is speculative but what would have authorized the department to do so is objective. "Termination" is being defined to eliminate confusion. Section 32-9-116, MCA, refers to actions that must be taken if a mortgage loan originator is "terminated." In this context, "terminated" does not mean fired for cause. It means separation from employment for any reason.

The department proposes to define "employing" to clarify that a mortgage loan originator employed by a single entity must be a W-2 employee of the entity. It has been common in the past for mortgage loan originators to be independent contractors for a company. This concept is inconsistent with the amendments to the Act required by the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (S.A.F.E. Act). Section 32-9-129, MCA, provides that a loan processor or

underwriter who is an independent contractor may not engage in mortgage loan originator activities unless licensed. To be licensed, the mortgage loan originator must be employed by one mortgage broker or one mortgage lender. Section 32-9-116, MCA. The mortgage broker or mortgage lender entity is responsible for the conduct of its mortgage loan originators. The designated manager is responsible for the conduct of the mortgage loan originators at the location at which the designated manager is the manager. Section 32-9-122, MCA. The amendments to the Act, read as a whole, make it clear that the legislative intent was to ensure that the entity is responsible for its employees' actions. Therefore, mortgage loan originators can no longer be independent contractors who are not subject to the control of the entity for whom they work.

The department proposes to amend the definition of "work in a related field" to reflect that an individual can no longer be licensed as a mortgage broker but only as a mortgage loan originator and that the three years of experience that was formerly a qualification for individual mortgage broker licensure will now qualify an individual to be identified as a designated manager under the Act. In addition, since under 32-9-109, MCA, "work in a related field" and "in a related field" mean the same thing, both phrases are being used in the definition.

The department proposes to amend the definition of "work in a related field" to include work as a mortgage loan officer at a financial institution. Under the Act, individuals working as registered mortgage loan originators for financial institutions (as a mortgage loan officer) are considered to be qualified by that experience to be a licensed mortgage loan originator working for a mortgage broker or mortgage lender.

2.59.1703 TRANSFER OF LOAN ORIGINATOR OR MORTGAGE BROKER LICENSE (1) Transfer of an individual mortgage ~~broker or~~ loan originator license must be approved by the department. To transfer an individual mortgage ~~broker or~~ loan originator license, the individual mortgage ~~broker or~~ loan originator shall obtain a relocation application from the department. The completed relocation application must be accompanied by a nonrefundable processing fee of \$50.

(a) remains the same.

(b) If the lapse in employment occurs over a renewal period, the individual mortgage ~~broker or~~ loan originator license must be renewed as required by 32-9-117, MCA, to qualify for a transfer of the license. The relocation six-month time frame would remain in effect and would be from the date of termination from the previous licensed entity.

(2) If an individual mortgage ~~broker or~~ loan originator is terminated by a mortgage broker or lender, and within six months is re-employed by the same mortgage broker or lender, a request for reinstatement form must be filed with the department. The form is available from the department. There is a \$10 processing fee for reinstatement. If the break in employment occurs over a renewal period, the individual mortgage ~~broker or~~ loan originator license must be renewed as required by 32-9-117, MCA, to qualify for reinstatement. The six-month time frame would remain in effect and would be from the date of termination.

AUTH: 32-9-130, MCA

IMP: ~~32-9-115~~, 32-9-116, 32-9-117, ~~32-9-119~~, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to amend this rule to reflect that under the Act, an individual can only be licensed as a mortgage loan originator, not as a mortgage broker. An individual mortgage loan originator may work for either a mortgage broker or a mortgage lender entity.

2.59.1705 LICENSING EXAMINATION AND CONTINUING EDUCATION PROVIDER REQUIREMENTS (1) remains the same.

(2) To receive approval of a ~~licensing examination or~~ continuing education course, the ~~examination or~~ course provider must file an application with the department, which includes, but is not limited to the following items:

(a) remains the same.

(b) a complete list of all examiners or instructors for the course, including their qualifications and experience with ~~examinations and~~ teaching courses similar to the course submitted for approval;

(c) a complete set of the ~~examination or~~ curriculum materials. Materials will be retained by the department. Electronic format is acceptable;

(d) through (4) remain the same.

(5) Courses and ~~licensing examinations~~ must reflect the activities performed by ~~applicants or~~ licensees and must provide ~~applicants or~~ licensees with a basic knowledge of and competency in any of the following:

(a) through (d) remain the same.

(e) the Montana Mortgage Broker, Mortgage Lender, and Mortgage Loan Originator Licensing Act;

(f) and (g) remain the same.

~~(6) Appropriate subjects for licensing examinations may include:~~

~~(a) the Montana Mortgage Broker and Loan Originator Licensing Act;~~

~~(b) state and federal consumer protection acts;~~

~~(c) the federal Real Estate Settlement Procedures Act, Truth in Lending Act, Equal Credit Opportunity Act, Fair Credit Reporting Act, Fair Housing Act, Home Mortgage Disclosure Act, Community Reinvestment Act, and the regulations promulgated pursuant to these acts;~~

~~(d) trust account and recordkeeping requirements of the Montana Mortgage Broker and Loan Originator Licensing Act;~~

~~(e) real estate and appraisal law;~~

~~(f) arithmetical computation common to mortgage lending, including but not limited to:~~

~~(i) the computation of an annual percentage rate;~~

~~(ii) finance charges;~~

~~(iii) amount financed;~~

~~(iv) payment and amortization;~~

~~(v) credit evaluation; and~~

~~(vi) calculating debt-to-income; and~~

~~(g) ethics in the mortgage industry.~~

(7) remains the same, but is renumbered (6).

~~(8)~~ (7) The provider shall file an application with the department that includes a copy of examinations to be used, if any, in determining satisfactory comprehension

of the contents of the course and the grading scale to be used. Any new or revised courses, examinations, or grading scales to be used shall be submitted to the department for approval at least 60 days prior to use. Course materials may be submitted in electronic format. The department will consider examinations and continuing education disseminated by written or electronic means, including by the internet.

~~(9)~~ (8) The department shall review applications filed and determine whether to approve or deny the proposed provider. If the department approves the course or provider, the department shall issue a certificate of approval that will be effective ~~for two years from the date of issuance~~ until NMLS approves the continuing education courses and providers.

(10) and (11) remain the same, but are renumbered (9) and (10).

~~(12)~~ (11) The department may audit an approved course ~~or examination~~ at any time. If the course provider ~~or examination administrator~~ has not complied with the requirements of this rule, the department may suspend or terminate the approval and require the surrender of the certificate of approval.

(13) through (20) remain the same, but are renumbered (12) through (19).

AUTH: 32-9-130, MCA

IMP: ~~32-9-110~~, 32-9-118, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to remove references to prelicense testing from this rule because the S.A.F.E. Act requires that the NMLS approve and administer prelicense testing. Title V of the Housing and Economic Recovery Act of 2008 (Pub. L. 110-289, 1501-1517, 122 Stat. 2654, 2810-2824 [July 30, 2008]), and 32-9-110, MCA.

Certificates of approval issued to course providers after the effective date of these amendments will remain valid until the NMLS assumes the function of administering and approving continuing education courses. It is not known at this time when that will occur.

The department also proposes to reflect the revised name of the Act.

2.59.1706 IRREVOCABLE LETTER OF CREDIT OR SURETY BOND ~~(1) If using an irrevocable letter of credit, the letter of credit shall be from a financial institution acceptable to the department. The entity name on the application and on the irrevocable letter of credit must match exactly.~~

~~(2)~~ (1) If using a surety bond, ~~the~~ the surety bond shall be issued by a surety company authorized to do business in the state of Montana. The bond, including any and all riders and endorsements executed subsequent to the effective date of the bond, shall be placed on file with the department. The entity name on the application and on the surety bond must match exactly. The bond shall be continuous and may be cancelled by the surety upon the surety giving 30 days written notice to the department of its intent to cancel the bond. Whether or not the bond is renewed, continued, reinstated, reissued, or otherwise extended, replaced, or modified, including increases or decreases in the penal sum, it shall be considered one continuous obligation, and the surety upon the bond shall not be

liable in an aggregate or cumulative amount exceeding the penal sum set forth on the face of the bond.

~~(3) The department or any person injured by a violation of this act may bring an action in a court of competent jurisdiction against the surety bond or approved alternative of the licensed mortgage broker who committed the violation or who employed or engaged the loan originator who committed the violation.~~

~~(a) An action against an irrevocable letter of credit must be commenced within one year after the expiration date of the relevant letter of credit or one year after the cause of action accrues, whichever occurs later. A cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach.~~

~~(b) In the event valid claims of borrowers and bona fide third parties against a bond or irrevocable letter of credit exceed the amount of the bond or deposit, each claimant shall only be entitled to a pro rata amount, based on the amount of the claim as it is valid against the bond or irrevocable letter of credit, without regard to the date of filing of any claim or action.~~

~~(c) A judgment arising from a violation of the Montana Mortgage Broker and Loan Originator Licensing Act or a rule adopted under that act shall be entered for actual damages and in no case be less than the amount paid by the borrower to the licensed mortgage broker plus reasonable attorneys' fees and costs. In no event shall the surety bond or approved alternative provide payment for any trebled or punitive damages.~~

~~(d) Borrowers and bona fide third parties shall be given priority over the department and other persons in distributions in actions against the surety bond.~~

~~(2) The rRemedies relating to the bond provided under this rule are cumulative and nonexclusive and do not affect any other remedy available at law.~~

AUTH: 32-9-130, MCA

IMP: 32-9-123, MCA

STATEMENT OF REASONABLE NECESSITY: The S.A.F.E. Act requires the state regulatory authority to establish a net worth or surety bond requirement for mortgage loan originators based on the dollar amount of loans originated by the mortgage loan originator. Section 32-9-123, MCA, implements the provisions of the S.A.F.E. Act and no longer allows letters of credit to be used in lieu of a surety bond. Therefore, the department proposes to remove all references to letters of credit from this rule.

Section 32-9-123, MCA, does not allow the department to bring an action on a surety bond on its own behalf, nor does it allow an injured person to bring an action against the bond. The department proposes to repeal (3) of this rule because it does not comply with 32-9-123, MCA.

Section 32-9-123, MCA, does not address the matters in (3); therefore, this section is being proposed to be repealed.

2.59.1707 REVOCATION, SUSPENSION, OR SURRENDER OF LICENSE

(1) A licensee may offer to surrender a license by delivering to the department written notice of the offer of surrender. ~~but a~~ An offer of surrender or

accepted surrender does not affect the licensee's civil or criminal liability for acts initiated or committed before the surrender while licensed.

(2) The department may refuse to accept the offer of surrender of a license if:

(a) a final order has been issued in an enforcement action and the licensee has not fully complied with the order regardless of whether compliance is yet due;

(b) the licensee has violated, or is under investigation for a suspected violation of, the Montana Mortgage Broker, Mortgage Lender, and Mortgage Loan Originator Licensing Act or any rule in this subchapter;

(c) there is an enforcement action or complaint pending against the licensee;
or

(d) the licensee has not made arrangements satisfactory to the department regarding loans in process at the time of the offer of surrender.

(2) remains the same, but is renumbered (3).

(3) (4) In the event of a revoked, suspended, or surrendered mortgage broker, mortgage lender, or loan originator license, no fees will be refunded by the department.

AUTH: 32-9-130, MCA

IMP: 32-9-126, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to amend this rule to reflect the new categories of licensees under the Act. Under the Act, an entity may be licensed as either a mortgage lender or mortgage broker. An individual may be licensed only as a mortgage loan originator.

Recently, the department has experienced several licensees, who, when they discovered they were under investigation for an alleged violation of the Act, surrendered their licenses. After surrendering the license, the entity did not pay fines imposed by department order as a penalty for violation of the Act. While technically the fine may not have been imposed or been due before the surrender of the license, the department believes the purpose of the offer of surrender was to evade prosecution and punishment for acts that were alleged to violate the Act. With the advent of the NMLS, all states will have immediate access to every other state's disciplinary actions against a particular licensee. This will increase the incentive for licensees to evade disciplinary action by surrender of a license. In order to prevent this evasion, the department must have the authority to refuse to accept a proffered surrender of a license if the department has reason to believe that the licensee seeks to evade some provision of the Act.

Recent experience has shown that lenders or brokers who suddenly surrender their licenses either to attempt to evade enforcement actions or due to adverse economic conditions, often have loan applications in process. Loans in process are loans in which an application has been taken, but the loan has not yet closed and funded. If a lender or broker ceases doing business suddenly, the borrowers who paid fees such as credit report fees or application fees will lose their money, or lenders will proceed to close and fund the loans without a license. The department views both of these alternatives as unacceptable. A lender or broker that ceases doing business must make arrangements for the loan to be taken over by a licensed entity so that the borrowers do not lose money and the loans are

completed by a licensed entity. In order to ensure that this happens, the department must be able to refuse the surrender of the license until appropriate arrangements have been made for loans in process.

2.59.1709 CONSUMER COMPLAINT PROCESS (1) A complaint form will be provided by the department. A complaint must be submitted in writing to the department. If the basis of the complaint relates to the Montana Mortgage Broker, Mortgage Lender, and Mortgage Loan Originator Licensing Act, it will be investigated by the department or designated party.

AUTH: 32-9-130, MCA

IMP: 32-9-130, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to amend this rule to reflect the revised title of the Act.

2.59.1710 RECORDS TO BE MAINTAINED BY MORTGAGE BROKERS

(1) through (1)(m) remain the same.

(2) A mortgage broker shall maintain ~~at its principal Montana location~~ a trust account records file showing a sequential listing of checks written for each bank account relating to the licensee's business as a mortgage broker, showing at a minimum, check number, the payee, amount, date, and purpose of payment or deposit, including identification of the loan to which it relates, if any. The licensee shall reconcile the bank accounts monthly.

(3) through (3)(i) remain the same.

(j) the name of the individual mortgage ~~broker~~ or loan originator who originated the loan.

AUTH: 32-9-130, MCA

IMP: 32-9-121, 32-9-124, 32-9-125, MCA

STATEMENT OF REASONABLE NECESSITY: The Act repealed the brick-and-mortar requirement for licensees that existed under prior law. So, the department proposes to delete the phrase "at its principal Montana location" from this rule to comply with current law.

Mortgage brokers are entities under 32-9-103(21), MCA. Individuals are mortgage loan originators. The department, therefore, is deleting broker in reference to an individual to comply with current law.

4. The department proposes to repeal the following rules:

2.59.1704 LICENSE RENEWAL, found on ARM page 2-6134.

AUTH: 32-9-130, MCA

IMP: 32-9-115, 32-9-116, 32-9-117, 32-9-118, 32-9-123, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to repeal ARM 2.59.1704 because new rules are being proposed in this rulemaking which create temporary licenses for mortgage lenders whose current licenses expire on September 30, 2009. Under the Act, current licensees holding a valid license as of July 1, 2009, must be licensed through the National Mortgage Licensing System (NMLS) by June 30, 2010. Mortgage lender entities holding a valid license as of July 1, 2009 must have the ability to continue to conduct business after their current licenses expire under a temporary license that will run from its issuance date until the entity becomes licensed through NMLS.

As of July 1, 2009, mortgage loan originators working for mortgage lenders must be individually licensed. Section 32-9-102, MCA. Prior Montana law did not require individuals working for licensed lenders to be licensed. NEW RULE II is being proposed in this rulemaking to allow mortgage loan originators working for mortgage lenders to be temporarily licensed until they become licensed through NMLS or April 1, 2010, whichever is earlier.

Section 32-9-105(4), MCA, provides that all new applicants after July 1, 2009, must be licensed through the NMLS by April 1, 2010. Licensees with current licenses as of July 1, 2009, must be licensed through the NMLS by June 30, 2010.

2.59.1711 CONTINUING EDUCATION, found on ARM page 2-6142.

AUTH: 32-9-130, MCA

IMP: 32-9-130, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to repeal ARM 2.59.1711 because the S.A.F.E. Act requires all mortgage loan originators to meet certain minimum standards including continuing education. The S.A.F.E. Act requires that continuing education courses be taken in certain areas and controls the timeframe for taking continuing education credits. When the department transitions to the NMLS, the department will no longer be approving continuing education courses or providers. The continuing education credits must be submitted to the NMLS, not the department, in order for the applicant to become licensed through the NMLS.

2.59.1712 DESIGNATED MANAGERS, found on ARM page 2-6143.

AUTH: 32-9-130, MCA

IMP: 32-9-103, 32-9-122, MCA

STATEMENT OF REASONABLE NECESSITY: 32-9-122, MCA, defines designated manager and sets forth the responsibilities of a designated manager. Therefore, the department proposes to repeal ARM 2.59.1712 as it would unnecessarily repeat the statute.

2.59.1713 EXAMINATIONS, found on ARM page 2-6143.

AUTH: 32-9-130, MCA

IMP: 32-9-130, MCA

STATEMENT OF REASONABLE NECESSITY: Section 32-9-141, MCA provides that for the purpose of investigations, complaints, or examinations the department may review, investigate, or examine any licensee or person subject to the Act. Therefore, the department proposes to repeal ARM 2.59.1713 as it unnecessarily repeats the statute.

2.59.1715 GROUNDS FOR THE DENIAL OF AN APPLICATION, as found on ARM page 2-6144.

AUTH: 32-9-130, MCA

IMP: 32-9-115, 32-9-116, 32-9-130, MCA

STATEMENT OF REASONABLE NECESSITY: The department proposes to repeal ARM 2.59.1715 because 32-9-120, MCA, makes a material misstatement of fact or material omission of fact in the application grounds to deny the license or renewal. ARM 2.59.1715 unnecessarily repeats the statute.

5. The proposed new rules provide as follows:

NEW RULE 1 LICENSE RENEWALS FOR MORTGAGE LENDERS LICENSED AS OF JULY 1, 2009 - TEMPORARY LICENSES (1) A mortgage lender who held a valid license as a Montana residential mortgage lender as of July 1, 2009, and who applies for renewal of the license is eligible for a temporary license as provided in this rule.

(2) The term of the temporary license issued to a mortgage lender is from the date of issuance of the license until the earlier of:

(a) the granting of an unconditionally approved license status to the lender by Montana through the National Mortgage Licensing System (NMLS); or

(b) April 1, 2010.

(3) Mortgage lender applications for a temporary license must be submitted to the department by September 1, 2009, in order to assure the issuance of a temporary license to qualified renewal applicants before their current licenses expire on September 30, 2009. An application may be submitted after September 1, 2009, but if it cannot be processed in time for issuance of a temporary license by September 30, the renewal applicant's authority to engage in the business of mortgage lending expires on September 30 and incidences of unlicensed mortgage lender activity will be prosecuted by the department.

(4) An application for a temporary license must be submitted on a form prescribed by the department. Each mortgage lender shall license at least one main office and all branch offices at which Montana residential mortgage loans are originated. Each office must have a designated manager.

(5) The nonrefundable fee for a temporary mortgage lender license is \$375 for the main office and \$125 for each branch office.

(6) For each entity seeking temporary licensure as a mortgage lender, each of the persons listed in 32-9-113, MCA, shall submit an affidavit in a form prescribed

by the department swearing or affirming that they meet the requirements of 32-9-120(1)(a), (b), (c), and (g), MCA, as of the date of application.

(7) If an applicant for a temporary license does not maintain a physical office in Montana, the applicant must comply with 32-9-128, MCA.

AUTH: 32-9-114, MCA

IMP: 32-9-102, 32-9-105, 32-9-113, 32-9-120, 32-9-123, MCA

STATEMENT OF REASONABLE NECESSITY: Mortgage lenders were first licensed in Montana starting October 1, 2008. The licenses issued to mortgage lenders on or after October 1, 2008, expire on September 30, 2009. The Montana Residential Mortgage Lender Licensing Act found at 32-10-101 et seq., MCA, was repealed on July 1, 2009, when the Act became effective. Mortgage lenders who held a valid license as of July 1, 2009 will need a temporary license authorizing them to continue in business from October 1, 2009, until they become licensed by Montana through the NMLS, assuming the lender meets the criteria for licensure, or until June 30, 2010, whichever occurs first.

Formerly, loan originators working for licensed mortgage lenders were not required to be licensed. The Act requires that they become licensed. The implementation date for their licensure under NMLS is April 1, 2010. In order for a new applicant for loan originator licensure to qualify, the applicant must be employed by a licensed mortgage lender or licensed mortgage broker. This rule coordinates the licensure of mortgage lenders with the licensure of their loan originator employees so there need not be a gap or lapse in the ability of lenders and their loan originators to conduct business.

Mortgage lenders must be licensed on the NMLS by June 30, 2010; however, as a practical matter, mortgage lenders will have to transition on to NMLS and become licensed by Montana by April 1, 2010, in order to allow their loan originator employees to become licensed by April 1, 2010. Because of this, the term of the temporary license is from the date of issuance of the license to the earlier of April 1, 2010, or the granting of an unconditionally approved license status by the department through the NMLS.

The department will prorate the fee for this temporary license, which is available for six months, and charge one-half of the \$750 yearly fee for renewal. Section 32-9-117, MCA, provides that an applicant shall pay one-half of the initial nonrefundable fee for any license period of less than six months. Because that provision of the statute was not amended by the Act, the department has set the fee for the temporary license at one-half the yearly fee.

Lenders will have to meet the substantive requirements of the Act to be licensed. These include qualifications of ultimate equity owners and control persons of the entity, licensing of branches, and appointing the department as the registered agent for service of process if the lender does not have a physical presence in Montana. References to those statutory requirements are included in the rule in this instance to lessen the burden on applicants and licensees who are dealing with a great number of substantive changes relative to licensing at this time.

NEW RULE II NEW APPLICANTS FOR A MORTGAGE LOAN
ORIGINATOR LICENSE - TEMPORARY LICENSES

(1) An individual who does not hold a valid license as a Montana residential mortgage loan originator or mortgage broker as of July 1, 2009, may apply for a temporary license as provided in this rule on a form prescribed by the department.

(2) The term of the temporary license issued to a mortgage loan originator is from the date of issuance of the license until the earlier of:

(a) the granting of an unconditionally approved license status by Montana to the mortgage loan originator through the NMLS; or

(b) April 1, 2010.

(3) The nonrefundable fee for a temporary mortgage loan originator license is \$300.

(4) To be granted a temporary license, a mortgage loan originator applicant shall meet the requirements in 32-9-120(1)(a), (b), (c), (d), and (g), MCA.

(5) An applicant for a temporary mortgage loan originator license shall submit the information and documentation required by 32-9-127(1)(a), (b), and (c), MCA, to the department rather than to the NMLS.

(6) If an applicant for a temporary mortgage loan originator license does not maintain a physical office in Montana, the applicant shall comply with 32-9-128, MCA.

AUTH: 32-9-114, MCA

IMP: 32-9-102, 32-9-105, 32-9-120, 32-9-127, 32-9-128, MCA

STATEMENT OF REASONABLE NECESSITY: As of the July 1, 2009, (the effective date of the Act), all mortgage loan originators working for mortgage lenders have to be licensed to engage in origination activities in Montana. In addition, there must be a process by which an individual who was not licensed as of July 1, 2009, can become licensed until the individual is required to transition to NMLS and become licensed by Montana. This rule is intended to address these issues.

Since all individuals who did not hold a valid license as of July 1, 2009, must be licensed by Montana through the NMLS by April 1, 2010, the term of the temporary license must run from the date of its issuance to the earlier of the date when the individual is licensed by Montana through NMLS or April 1, 2010.

The division has set the fee for this temporary license at the rate for nine months of licensure. The annual fee for a mortgage loan originator license is \$400 pursuant to 32-9-117, MCA. The department has prorated the fee to cover the actual period of licensure, which is nine months.

To be granted a temporary license, the applicant shall meet the requirements of 32-9-120, MCA, regarding qualifications and the requirements of 32-9-128, MCA, regarding the appointment of the department as registered agent for service of process if the individual is not physically located in Montana.

Individuals shall comply with the background, fingerprinting, and credit report requirements in 32-9-127, MCA, to allow the department to make the determination as to whether the applicant meets the financial responsibility, character, and general fitness standards for licensure.

NEW RULE III NEW APPLICANTS FOR A MORTGAGE BROKER OR MORTGAGE LENDER LICENSE - TEMPORARY LICENSES (1) An entity that did not hold a valid license as a Montana residential mortgage lender or Montana mortgage broker as of July 1, 2009, may apply for a temporary license as provided in this rule on a form prescribed by the department.

(2) Each entity shall license at least one main office and all branch offices at which Montana residential mortgage loans are originated. Each office must have a designated manager.

(3) The term of the temporary entity license is from the date of issuance of the license until the earlier of:

(a) the granting of an unconditionally approved license status by Montana to the entity through the NMLS; or

(b) April 1, 2010.

(4) The nonrefundable fee for a temporary mortgage broker license is \$375 for the main office and \$187.50 for each branch office. The nonrefundable fee for a temporary mortgage lender license is \$562.50 for the main office and \$187.50 for each branch office.

(5) For each entity seeking temporary licensure as a mortgage lender or broker, each of the persons listed in 32-9-113, MCA, shall submit the information and documentation required by 32-9-127(1)(a), (b), and (c), MCA, to the department rather than to the NMLS.

(6) For each entity seeking temporary licensure as a mortgage lender or broker, each of the persons listed in 32-9-113, MCA, shall meet the requirements in 32-9-120(1)(a), (b), (c), and (g), MCA.

(7) Applicants shall submit proof of compliance with the requirements of 32-9-123, MCA.

(a) Entities that elect to purchase a surety bond shall purchase a surety bond for \$50,000 in order to receive a temporary license.

(b) If an applicant qualifies for the net worth requirement in lieu of surety bond, the entity shall comply with [New Rules IV, V, and VI].

(8) If an applicant for a temporary license does not maintain a physical office in Montana, the applicant shall comply with 32-9-128, MCA.

AUTH: 32-9-114, MCA

IMP: 32-9-102, 32-9-105, 32-9-113, 32-9-120, 32-9-123, 32-9-127, 32-9-128, MCA

STATEMENT OF REASONABLE NECESSITY: There must be a process by which an entity that was not licensed as of July 1, 2009, can become licensed until the entity transitions to the NMLS and becomes licensed by Montana through the NMLS. This rule is intended to establish that process.

Since all entities that did not hold a valid license as of July 1, 2009, must be licensed by Montana through the NMLS by April 1, 2010, the term of the temporary license must run from the date of its issuance to the earlier of the date when the entity is licensed by Montana through NMLS or April 1, 2010.

The department has prorated the annual fee for licensure of mortgage brokers, which is \$500 for a main office and \$250 for a branch, to cover the actual

period of licensure, which is nine months. The department has prorated the annual fee for licensure of mortgage lenders, which is \$750 for a main office and \$250 for a branch, to cover the actual period of licensure, which is nine months.

Each entity must show proof that they have met the requirements of 32-9-123, MCA. The department has set the initial bonding amount at \$50,000. When the applicant applies for licensure through the NMLS, the applicant will be required to document the annual loan production for each of its mortgage loan originators and the surety bond amount will be set based on the annual loan production volume for all mortgage loan originators working for the entity the year preceding licensure. However, to lessen the burden on applicants and for the sake of clarity during the temporary licensing period, the department has elected not to require the submission of annual loan production volume and has instead set the bond at the middle range for bonds, that being \$50,000. If the mortgage broker entity elects to utilize the net worth requirement in lieu of a surety bond, it must comply with [New Rules IV, V, and VI].

NEW RULE IV NET WORTH REQUIREMENT FOR MORTGAGE BROKERS

(1) If a mortgage broker chooses to utilize the net worth requirement in lieu of a surety bond, the mortgage broker shall maintain an adjusted net worth of assets acceptable to the department of the following amounts:

- (a) \$250,000 based on a loan production of less than \$50 million per year;
 - (b) \$500,000 based on a loan production of \$50 million but less than \$100 million per year;
 - (c) \$1 million based on a loan production of more than \$100 million per year.
- (2) The mortgage broker shall maintain liquid assets of 20% of its adjusted net worth or \$50,000, whichever is less.

(3) Liquid assets are cash and cash equivalents.

(a) Cash includes cash on hand, checking accounts, savings accounts, certificates of deposit (net of any early withdrawal penalty), and other cash equivalents with a federally-insured financial institution.

(b) Cash equivalents are readily marketable assets. Cash equivalents include but are not limited to:

- (i) United States government securities at market value; and
- (ii) stocks and bonds actively traded on a national United States security exchange with certificates issued in the name of the mortgage broker. These assets will be accepted at 90% of their 52-week low, as reflected at the time of submission of the audit.

(c) To be considered a liquid asset, the cash or cash equivalent must not be restricted or otherwise reserved for any purpose other than the payment of a current liability.

(d) A line of credit or letter of credit is not a liquid asset. Loans held for resale by the mortgage broker are not considered liquid assets.

(4) The computation of adjusted net worth is required for all mortgage brokers who utilize the net worth requirement, even if no loans were originated or serviced during the previous 12-month period. The required adjusted net worth must be maintained throughout the year. When the mortgage broker is a parent or a subsidiary of a parent, the adjusted net worth computation must focus on the assets

and liabilities of the individual entity with the net worth requirement, not the consolidated adjusted net worth of both entities.

(5) In calculating the adjusted net worth, the assets listed in [New Rule V] are unacceptable assets.

AUTH: 32-9-114, MCA

IMP: 32-9-123, MCA

STATEMENT OF REASONABLE NECESSITY: Section 32-9-123(3), MCA, states that in lieu of a surety bond, a mortgage broker may meet a minimum net worth requirement. That option has not been available in the past. The goal of the department in drafting these new rules is to fairly reflect assets that should count toward a net worth requirement. The net worth requirement is designed to protect borrowers or third parties who are financially injured by an act of a mortgage broker or loan originator. And, as we have seen recently with the implosion of many national mortgage brokers, even a high net worth can be fleeting. Therefore, the department seeks to ground its net worth requirement in actual assets with real value, not speculative or transient assets. The net worth requirement is based on the federal requirements for approval by the Department of Housing and Urban Development (HUD) to originate Federal Housing Administration home loans and the requirements for surety bonds or assets in lieu of bonds used by the federal government under the Federal Acquisition Regulation System.

[New Rule IV] set the minimum net worth for mortgage brokers based on the dollar amount of loans originated per year. The scaling of the net worth requirement to loan production volume is required by 32-9-123(2)(b), MCA, and the S.A.F.E. Act, 12 U.S.C. 1508(d)(6). The loan production period is one year because mortgage brokers are required to be licensed annually under 32-9-117, MCA, and the S.A.F.E. Act, 12 U.S.C. 1504 (a)(1).

Customarily, a portion of a net worth requirement must be held in liquid assets. In this case, the department has determined that a sufficient liquidity for net worth purposes is 20% of the adjusted net worth or \$50,000, whichever is less. This is based on a similar requirement by HUD for supervised and nonsupervised mortgagees or loan correspondents. HUD requires that 20% of the adjusted net worth to be held in liquid assets. The department believes, based on its knowledge of its licensees, that 20% liquidity is sufficient to protect borrowers and allows licensees to function properly.

The classification of assets as cash or cash equivalents is based on the federal requirements for approval by the HUD to originate Federal Housing Administration home loans and the requirements for surety bonds or assets in lieu of bonds used by the federal government under the Federal Acquisition Regulation System. The department believes that cash should include cash on hand, as well as amounts in checking and savings accounts. In addition, cash is defined to include certificates of deposit as long as any early withdrawal penalties are deducted to reflect the amount of cash that would be received if the certificate of deposit were cashed in early.

Cash equivalents are substantially the same as cash. A cash equivalent must be readily convertible into cash. Government securities, like treasury bills, treasury

notes, treasury bonds, savings bonds, and zero coupon government bonds, are examples of cash equivalents. Because there is a readily definable and accessible market for these securities which does not vary widely, they are accepted at market value. Other stocks and bonds that are traded on a national United States security exchange are also acceptable as cash equivalents. However, since the market value of these securities can vary widely over time, they are accepted at 90% of their 52-week low value.

Credit cannot be an asset since it must be repaid. Nor can assets that are pledged elsewhere count toward net worth. Loans held for resale by a mortgage broker are not a liquid asset since they are held only briefly until they can be sold, not as an asset of the mortgage broker.

Since the net worth requirement is designed to protect borrowers and third parties who suffer a loss as a result of an act of the mortgage broker or loan originator, the net worth requirement must be maintained at all times throughout the year not just at renewal of the license and must be calculated while the mortgage broker is licensed, even if no loans were originated or serviced during that period.

NEW RULE V UNACCEPTABLE ASSETS (1) The following are unacceptable assets and may not be used in the computation of adjusted net worth:

- (a) any asset or portion of an asset pledged to secure obligations of another mortgage broker, entity, or any person;
- (b) an asset due from a control person or ultimate equity owner of the mortgage broker, from a related entity, their family members, or a related entity in which the control person or ultimate equity owner or family member has a financial or managerial interest;
- (c) a business venture in an unrelated entity;
- (d) the portion of an investment that reflects the ownership interest of the mortgage broker in a joint venture, affiliate, and/or other related entity which is carried at a value greater than equity, as adjusted. "Equity as adjusted" means the book value of the related entity reduced by the amount of unacceptable assets carried by the related entity;
- (e) any intangible asset, such as goodwill, covenants not to compete, franchise fees, organizational costs, value placed on insurance renewals, or value placed on property management contract renewals;
- (f) the value of any servicing contract not determined in accordance with Statement of Financial Accounting Standards (SFAS) No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities;"
- (g) any asset not readily marketable and for which appraised values are very subjective. Examples include, but are not limited to, antiques, artwork, and gemstones;
- (h) any amount in excess of the estimated realizable or recovery value of mortgages in foreclosure, constructions loans, or property acquired through foreclosure based on the value of the appraisal at the time of foreclosure reduced by taxes, insurance, expenses of sale, and improvements to the property;
- (i) any asset that is principally used for the personal enjoyment or benefit of a control person or ultimate equity owner and not for normal business purposes. This

includes automobiles and personal residences. "Principally used" means that any other use of the property must be solely incidental;

(j) that portion of contributed property, not otherwise excluded, in excess of the value as of the date of contribution determined by an independent appraiser;

(k) notes that have been 60 days or more delinquent in payments two or more times in the past two years or accounts receivable that are more than 30 days past due;

(l) foreign securities which are not traded on a United States security exchange;

(m) real property as follows:

(i) real property located outside the continental United States and its outlying areas;

(ii) real property that is a principal residence of a control person or ultimate equity owner;

(iii) real estate held for sale or investment if development will not start within two years from date of acquisition;

(iv) real property owned concurrently regardless of the form of cotenancy (including joint tenancy, tenancy by the entirety, and tenancy in common) except where all cotenants agree to act jointly; and

(v) life estates, leasehold estates, leasehold improvements, or future interests in real property;

(n) personal property;

(o) lines of credit or letters of credit; and

(p) speculative assets such as mineral rights.

AUTH: 32-9-114, MCA

IMP: 32-9-123, MCA

STATEMENT OF REASONABLE NECESSITY: Since the net worth requirement is designed to protect borrowers and third parties who suffer a loss as a result of an act of the mortgage broker or loan originator, the department has excluded certain assets that, in the experience of the financial examiners in the department, can be exaggerated or inflated to make a net worth appear to be greater than it actually is.

This rule identifies types of assets unacceptable to the department because their values are susceptible of being overstated. The unacceptable assets are based on the federal requirements for approval by HUD to originate Federal Housing Administration home loans.

NEW RULE VI PROOF OF NET WORTH (1) The applicant shall submit its most current certified public accountant-prepared audited financial statements for the period not more than 12 months prior to the submission of the application. The financial statements must be supplemented by a computation of adjusted net worth pursuant to this subchapter.

(2) All financial statements must be prepared in accordance with generally accepted accounting principals (GAAP). The audit must be performed in accordance with generally accepted auditing standards (GAAS) by a certified public

accountant authorized to perform audits in this state. The audit must be complete, original, and contain the auditor's report on the audit firm's letterhead stationery.

(3) Values of real property must be supported by an appraisal within the previous 12 months by an independent appraiser with the correct certification and licensure to give an accurate appraisal of the value of the property.

(4) For an ongoing business concern, a full set of financial statements is required including:

- (a) balance sheet;
- (b) income statement;
- (c) cash flow statement;
- (d) retained earnings statement;
- (e) footnotes; and
- (f) auditor's report containing an unqualified (clean) opinion.

(5) If the applicant is a new company and has had no revenues or cash flow, the income statement and cash flow statement are not required.

AUTH: 32-9-114, MCA

IMP: 32-9-123, MCA

STATEMENT OF REASONABLE NECESSITY: To ensure that the net worth requirement is adequately calculated and documented, the department will require CPA-prepared audited financial statements and computation of adjusted net worth. The financial statements must be prepared in accordance with generally accepted accounting principals using generally accepted accounting standards by a CPA. The proof of net worth rule is based on the federal requirements for approval by HUD to originate federal home loans.

To verify the valuation of property, an appraisal by a licensed appraiser with sufficient expertise in the particular area of appraising is required which must be within the audit period. The point of requiring accurate and independently verified valuations is to ensure that net worth is what the entity claims it is.

Since it is impossible to determine net worth without a full set of financial statements, full financial statements are being required, except in the case of start-up companies that do not have revenues or cash flow – they obviously cannot complete an income statement or cash flow statement.

NEW RULE VII RECORDS TO BE MAINTAINED BY MORTGAGE LENDERS (1) All licensees shall maintain and preserve financial records concerning business operations, transactions with customers, and escrow account transactions.

(2) Any books, accounts, or records required to be maintained by the department may be maintained in paper, electronic, or digital format approved by the department provided the records shall be made available to the department as required by the statutes and rules, and at the request of the department, the records shall be printed or transferred to a format that is usable by the department.

(3) A mortgage lender shall create and maintain the following records:

- (a) copies of all disclosures required by 32-9-148, MCA;

(b) copies of all payroll records, including federal and state withholding tax forms, W-2s, and 1099 forms filed with the Internal Revenue Service by the licensee or its agent on behalf of individuals employed by the licensee or on behalf of individuals acting as independent contractors in the mortgage lending business;

(c) a general ledger and subsidiary records sufficient to produce, when requested by the department, an accurate monthly statement of assets and liabilities, and a cumulative profit and loss statement for the current operating year;

(d) all checkbooks, bank statements, deposit slips, and cancelled checks that pertain to the mortgage lending business of the licensee;

(e) supporting documentation for all expenses and fees paid by the mortgage lender on behalf of the customer; and

(f) copies of all credit report bills received from all credit reporting agencies for the most recent five-year period.

(4) Mortgage lenders shall maintain an employee file for each employee that contains all documents related to the hiring of the employee, including name, date of birth, position or title and responsibilities, starting date, and date and reason for termination of employees. For purposes of this rule, employee shall include employees, independent contractors, and consultants who are involved in loan origination, loan servicing, loan negotiations, investor solicitation, or who transact business with borrowers or lenders.

(5) Financial records must include, at a minimum:

(a) a record of all monies received from borrowers, such as a cash receipts journal, showing at least:

(i) name of payor;

(ii) date of receipt;

(iii) amount received;

(iv) purpose of receipt including identification of the loan to which it relates, if any; and

(v) disposition of all monies received including the date and place of deposit or, if not deposited, the date, name of the person who received the monies, and the manner in which the monies were transmitted;

(b) a sequential listing of all checks written for each bank account relating to the licensee's business, such as a cash disbursement journal, showing at least:

(i) name of the payee;

(ii) date of payment;

(iii) amount of the payment; and

(iv) purpose of the payment including identification of the loan to which it relates, if any;

(c) bank account activity source documents for every account maintained for the licensee's business including at least:

(i) receipted deposit tickets and if "less cash deposits" are made, an explanation of the use of the cash;

(ii) paid checks if available and if these items are truncated, a copy of a document authorizing the department to request and receive copies of processed items from the financial institution;

(iii) bank advices, including, but not limited to, debit and credit notices and overdraft notices; and

- (iv) monthly or periodic statements;
- (d) detail on wire transfers into or out of the account(s) including:
 - (i) the name of the person who is the payor or payee;
 - (ii) date;
 - (iii) amount;
 - (iv) purpose of receipt or payment; and
 - (v) identification of the loan to which it relates, if any; and
- (e) a record or file of all monies owed by the licensee, such as an accounts payable journal.

(6) Mortgage lenders shall maintain all borrower and investor complaints except complaints unrelated to borrower or investor transactions. Complaint files shall include:

- (a) copies or originals of all written complaints by borrowers and investors maintained in a separate complaint file by the individual's name in alphabetical order;

- (b) a copy of the response;
- (c) copies of correspondence related to the complaints; and
- (d) a written disposition of the complaint.

(7) Mortgage lenders shall maintain residential borrower files that must include:

- (a) a copy of each loan application form;
- (b) a copy of each executed fee agreement, if prepared;
- (c) in the case of residential or single family loans, a borrower acknowledged statement that a loan interest rate will float;
- (d) a copy of the executed lock agreement, if used. The lock agreement must specify at a minimum:

- (i) the date of the agreement;
- (ii) the file identification and property address;
- (iii) the lock-in rate;
- (iv) the lock expiration date;
- (v) a disclosure that the lock may be subject to change if any of the loan factors change;

- (vi) the loan type (fixed, adjustable rate mortgage, other); and
- (vii) a disclosure that if the lock expires, the rate and points are subject to change;

- (e) the term of the loan;
- (f) the loan fee and discount, if any;
- (g) copies of all good faith estimates prepared pursuant to Regulation X (24 C.F.R. 3500);

- (h) a copy of the executed authorization to release credit information form;
- (i) a copy of final credit report, or the report relied upon for the loan decision, if other than the final credit report, received on the borrower including documentation of borrower payment history;

- (j) all documents relating to the credit, underwriting, and pricing decisions of each loan file irrespective of whether the application has been denied, approved, or withdrawn;

- (k) all notes and comments by anyone working on the loan file;

(l) a copy of the truth in lending disclosure statements made pursuant to Regulation Z (12 C.F.R. 226);

(m) a copy of the final U.S. Housing and Urban Development (HUD) settlement statement;

(n) a copy of all denial letters;

(o) a copy of all appraisals; and

(p) a copy of all disclosures, handbooks, and pamphlets required by federal law.

(8) Advertising records must be maintained for five years following the last date of publication of the advertisement. All licensees shall maintain copies of:

(a) all printed advertising published in newspapers, magazines, newsletters, or other media designed for mass distribution; and

(b) scripts, or audio- and videotapes, for advertising broadcast on radio or television.

(9) Escrow account records must be maintained as follows:

(a) a licensee shall deposit all trust funds received from a client into the escrow depository and shall keep such funds in the escrow depository until the written escrow instructions agreed to by all parties have been fulfilled;

(b) a licensee shall not commingle any monies received from a client for deposit into an escrow account with personal funds of the licensee. For purposes of this rule, the following shall not constitute commingling of trust funds with personal funds provided the funds are removed from the trust account within 30 days:

(i) earned, but untransferred, interest income accruing to the licensee pursuant to a written agreement with the client; or

(ii) earned, but untransferred, fees due the licensee;

(c) every deposit into a neutral escrow depository shall be accompanied by a letter of transmittal that shall include a written notation of the file identification assigned to the transaction on whose behalf the deposit is made. Compliance with this rule may be satisfied when a licensee has attached a copy of the client's check to the letter of transmittal.

(10) With respect to mortgage loans for which a commitment has been issued but the loan has not yet closed and funded, each mortgage lender shall maintain a pipeline report or reports, updated on a monthly basis, that provides the following information, both by state and in the aggregate:

(a) total number and dollar amount of such loans;

(b) type of loan (i.e., purchase money, refinance, etc.);

(c) total number and dollar amount of all such loans having a locked-in interest rate and total number and dollar amount of such loans whose interest rate is not locked in;

(d) the date the commitment was issued; and

(e) any fees collected from the borrower up to the date of commitment by any party to the mortgage transaction.

(11) For each line of credit to the lender, a mortgage lender shall maintain a report, or equivalent documentation, updated monthly, listing:

(a) each advancement of funds from the line of credit that reflects the date of the advancement;

(b) the name of the borrower;

- (c) the date that the mortgage loan closed; and
- (d) the date the funds were forwarded to satisfy its obligation for the advancement from the line of credit.

(12) Each mortgage lender shall maintain a list, by state, of the closing agents or attorneys that it uses that contains, at a minimum, the name, address, and telephone number of the closing agent or attorney.

(13) Mortgage lenders shall maintain a mortgage loan application log showing:

- (a) the first and last name of the borrower(s);
- (b) the property address (street, city, state, and zip code);
- (c) the phone number of the borrower(s);
- (d) the initial application date;
- (e) the date the credit report was requested for the borrower(s);
- (f) the loan amount;
- (g) the status of the loan (pending, closed, withdrawn, cancelled, denied);
- (h) the total fees received indirectly or directly by the mortgage lender at the closing of the loan;
- (i) the total fees paid to the mortgage loan originator;
- (j) the loan funding source;
- (k) the service release premium; and
- (l) the name of the individual mortgage loan originator who originated the loan.

(14) For borrower loans that are funded directly or indirectly by investors who are individuals, the following must be maintained by the lender:

- (a) a copy of the written evidence of obligation and the instrument creating the investor's lien or assignment of the lien;

- (b) a copy of documents evidencing that the instrument creating the lien or assignment has been recorded; and

- (c) copies of guarantees, surety agreements, any recourse agreements or guarantees, and correspondence related to any statements made to the investor or any investment made by the investor.

AUTH: 32-9-130, MCA

IMP: 32-9-121, 32-9-125, 32-9-145, MCA

STATEMENT OF REASONABLE NECESSITY: The department seeks to define the books and records that must be maintained by licensees in this rule. In general, a mortgage lender must maintain all records concerning business operations, transactions with customers, and escrow account transactions to enable the department to verify compliance with the Act. The department does not have a preference as to the format in which the records are kept as long as they are accessible to the department for examination purposes.

Mortgage lenders must create and maintain records of all disclosures required by 32-9-148, MCA, as well as payroll records for its employees and independent contractors. In addition, lenders must create and maintain records that would allow the department to produce an accurate monthly statement of assets and liabilities, and a cumulative profit and loss statement for the current operating year.

Typically, the department would do this in an examination of a mortgage lender. In addition, the lender must maintain all records that would allow the department to do an examination including all checkbooks, bank statements, deposit slips, and cancelled checks that pertain to the mortgage lending business of the licensee, and supporting documentation for all expenses and fees paid by the mortgage lender on behalf of the customer; and copies of all credit report bills received from all credit reporting agencies for the most recent five-year period. The latter is used by examiners to ensure that each credit report pull has been properly authorized as required by the Fair Credit Reporting Act.

Mortgage lenders will be required to maintain a file on each employee or independent contractor they hire which includes hire date and termination date. This will allow department examiners to ensure that all individuals who should be licensed are, in fact, licensed. In addition, department examiners will be able to locate and speak to the individuals who did certain relevant actions in relation to a file or an investigation.

Financial records are necessary to allow examiners to trace money received from borrowers as well as money spent by the lender to ensure the funds are being used properly and are not being comingled with operating funds of the lender or other accounts. Examiners review the complaints made by borrowers and investors to ensure that the lender is not violating any provision of state or federal law.

Residential mortgage loan files are, of course, critical to the examination process. The mortgage loan file should contain all documents that evidence the loan and decisions made relative to the loan as well as notes and comments entered by anyone working on the loan file. Federal law requires that certain disclosure be made on an accurate and timely basis. In order to prove the disclosures were made on a timely and accurate basis, copies of the documents must be retained in the file.

Advertising records must be maintained in order to allow the department's examiners to determine whether the prohibitions in 32-9-124(2)(f) through (i), MCA, have been violated.

Escrow account records must be maintained to allow the examiners to audit the account to ensure that escrows are being properly calculated and used and that escrow funds are not being comingled with other funds. The language of 32-9-145, MCA, already prohibits comingling of escrow funds with any other funds. However, it is necessary to repeat this language in this rule in order to make clear that two items are not considered comingling. They are: earned, but untransferred, interest due to the lender pursuant to a written agreement with the client and earned, but untransferred, fees due to the lender.

The pipeline report of loans for which a commitment has been made but which have not been funded or closed is used by examiners to review the loans in process.

If the lender goes out of business, the report is also used to ensure that loans in the pipeline are transferred to a properly licensed entity before they are closed. If a lender surrenders its license, loans in process cannot be closed by the unlicensed entity and must be transferred to a properly licensed entity before they can be completed.

Lines of credit are used by some lenders as a source of funding their loans. If a lender uses the line of credit to fund loans, the department checks to make sure the lender is properly advancing funds from a line of credit to fund the loans made.

In the event of a complaint or an investigation, the department needs to know which closing agent or attorney the lender uses. The department can then subpoena the closing agent or attorney with the files to further its investigation.

The mortgage loan application log is used by examiners as a tool in the examination process. It gives the examiners the universe of loans that a lender has made or considered making. It allows the examiners to quickly scan the loans made to determine whether any loan draws their attention or requires further investigation. The application log can also be used as an examination tool in that the examiners may choose to pull every third or fifth loan in order to review the loan files. Or examiners may focus on a particular type of loan, or a loan originator, or a borrower, depending on the purpose and focus of the examination.

Recently, the department has experienced problems with lenders that use individual investors as a funding source. These lenders are called "hard money lenders". The lenders either make a direct loan from investor to borrower or, in some cases, aggregate investor funds to make loans to various borrowers. The investors are often relying on the lender to determine the creditworthiness of the borrower and ensure that the investor will have adequate collateral for the loan. The investors often believe that the lender should be making all required disclosures for them and ensuring that their investment will be safe. In several recent cases, the lenders were not determining the creditworthiness of borrowers or the adequacy of the collateral. In some cases, it was clear that the investor thought they had a different security interest than what they actually had.

To prevent these problems, if a lender uses individual investors to fund loans, the lender will be required to provide the investor with copies of documents showing the lien and the recording of the lien. The lender will also be required to maintain all statements and inducements made to investors to get them to invest as well as agreements with or guarantees made to investors. This will allow the department to investigate complaints and determine if investors are receiving adequate security for their investments.

NEW RULE VIII FINANCIAL RESPONSIBILITY (1) An applicant is not financially responsible when the applicant has shown a disregard in the management of the applicant's own financial condition. A determination that an applicant has not shown financial responsibility may include but is not limited to:

- (a) current outstanding judgments, except judgments solely as a result of medical expenses;
- (b) current outstanding tax liens or other government liens and filings;
- (c) foreclosures within the past three years; or
- (d) a pattern of seriously delinquent accounts within the past three years.

AUTH: 32-9-130, MCA

IMP: 32-9-120, 32-9-127, MCA

STATEMENT OF REASONABLE NECESSITY: Sections 32-9-120, MCA, and 32-9-127, MCA provide that the department may not issue or renew a mortgage loan originator license if the applicant has failed to demonstrate financial responsibility, character, and general fitness to command the confidence of the community. In this new rule, the department seeks to define the types of financial matters that will disqualify an applicant from licensure. The department has selected the four matters set forth above because it believes that an individual with any of the four financial issues listed above do not warrant a finding of financial responsibility. The four matters set forth above were identified by the Conference of State Bank Supervisors as criteria that should operate to disqualify an applicant from licensure. The Conference of State Bank Supervisors is a group of all state bank supervisors that regulate mortgage loan originators. The Conference has issued guidance to all states in certain important areas in an attempt to develop uniform standards for mortgage loan originators.

The reason that financial responsibility is important is that mortgage loan originators receive uniform residential loan applications and credit reports from borrowers. These two documents contain essentially all the relevant financial information about a borrower including name, address, social security number, account numbers, balances and where accounts are held, and all debts and assets of an individual. If a mortgage loan originator were tempted to commit identity theft, these two documents would provide all the information necessary to do so.

In addition, mortgage loan originators receive borrower funds that are intended to pay for credit reports and appraisal fees. These borrower funds are required to be placed into a trust account to be used only for their intended purpose. A mortgage loan originator who lacked financial responsibility might be tempted to misuse those funds for personal purposes rather than using the funds for their intended purpose.

The department views ensuring the financial responsibility of applicants as one of its central obligations under the S.A.F.E. Act and the Act.

6. Concerned persons may present their data, views, or arguments, either orally or in writing, at the hearing. Written data, views, or arguments may also be submitted to Kelly O'Sullivan, Legal Counsel, Division of Banking and Financial Institutions, P.O. Box 200546, Helena, Montana 59620-0546; faxed to the office at (406) 841-2930; e-mailed to kosullivan@mt.gov, and must be received no later than 5:00 p.m., September 14, 2009.

7. Kelly O'Sullivan, Legal Counsel, Division of Banking and Financial Institutions, has been designated to preside over and conduct the hearing.

8. An electronic copy of this proposal notice is available through the department's web site at <http://doa.mt.gov/AdministrativeRules.asp>. The department strives to make the electronic copy of the notice conform to the official version of the notice, as printed in the Montana Administrative Register, but advises all concerned persons that if a discrepancy exists between the official printed text of the notice and

the electronic version of the notice, only the official printed text will be considered. In addition, although the department works to keep its web site accessible at all times, concerned persons should be aware that the web site may be unavailable during some periods, due to system maintenance or technical problems.

9. The Division of Banking and Financial Institutions maintains a list of interested persons who wish to receive notices of rulemaking actions proposed by this division. Persons who wish to have their name added to the mailing list shall make a written request which includes the name and mailing address of the person to receive notices and specifies that the person wishes to receive notices regarding division rulemaking actions. Such written requests may be mailed or delivered to Christopher Romano, Division of Banking and Financial Institutions, 301 S. Park, Ste. 316, P.O. Box 200546, Helena, Montana 59620-0546; faxed to the office at (406) 841-2930; e-mailed to cromano@mt.gov; or may be made by completing a request form at any rules hearing held by the department.

10. The bill sponsor contact requirements of 2-4-302, MCA, apply and have been fulfilled. Senator Jeff Essman, the primary bill sponsor of SB 351 (2009), was contacted on May 19, 2009, by U.S. mail.

By: /s/ Janet R. Kelly
Janet R. Kelly, Director
Department of Administration

By: /s/ Michael Manion
Michael Manion, Rule Reviewer
Department of Administration

Certified to the Secretary of State August 3, 2009.